

# CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 220

June 27, 1958

## DEPLETION: GROSS INCOME FROM THE PROPERTY (CEMENT)

### Syllabus:

In the case of cement the "gross income from the property" for the purpose of computing percentage depletion is to be determined upon the actual selling price of the cement.

For the income years ended January 31, 1954, 1955, and 1956, taxpayer, a producer of cement, claimed percentage depletion based on the value of the mineral, calcium carbonate, and the processes required in the manufacture of cement before any chemical change had taken place in the extracted mineral. Up to this point, the mineral is known as filter cake which is obtained by removing much of the water from the "slurry" which is then ready to be processed in the rotary kilns. After the mineral is conveyed to the rotary kilns it is heated, which reduces it to a dense clinker. This process affects a chemical change, transforming it from a crude mineral state, which after grinding is known as cement. Cement is synthetic, not a mineral.

Advice is requested as to whether in the case of cement the "gross income from the property" for the purpose of determining percentage depletion is to be determined upon the basis of the filter cake, i.e., before a chemical change occurs, or upon the basis of the actual selling price of the cement.

Section 24833, formerly Section 25121(c), provides in part that the allowance for depletion -- shall be -- in the case of -- calcium carbonates -- 10 percent -- of the gross income from the property during the income year -- .

Section 24834, formerly Section 25121(c)1. provides in part: "As used in Section 24833 'gross income from property' means the gross income from mining. 'Mining' includes not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products -- ."

In order to limit the depletion base, Federal Regulation 111, Section 29.23(m)-1(f), was amended on July 14, 1953, by T.D. 6031, to provide in part that the term "ordinary treatment processes" would not include treatment affecting a chemical change. This change was not made in Reg. 24121i(1), which otherwise corresponds to the Federal Regulation. Notwithstanding the Regulation, on May 14, 1957, in the case of Dragon Cement Company v. U. S., 244 F2d 513,

cert. denied 355 U.S. 833, the court concluded that a taxpayer is entitled to a percentage depletion deduction based upon its gross income from cement. The same result was also reached in the case of brick and tile clay.

U. S. v. Merry Brothers Brick & Tile Co., 242 F2d 708, cert. denied 355 U.S. 824.

In view of the above cases, percentage depletion in the case of cement and brick and tile clay is to be based upon the selling price, and in the case of brick and tile clay the selling price includes all operations up to and including the burning and the loading for shipment to customers.

In view of the fact that the Supreme Court has denied a hearing, and since the Internal Revenue Service has announced that it will not litigate the matter in subsequent cases, since the State and Federal laws in this respect are substantially the same, it is concluded that the decisions of the Dragon Cement Co. and Merry Brothers Brick & Tile Co. cases should be followed in this and subsequent cases.